

## **SECTION 2: CHINA'S PROLIFERATION PRACTICES AND RECORD**

### **Key Findings**

- China's proliferation activities are broad ranging; it continues to provide equipment and technology, including dual-use goods and technologies, related to WMD and their delivery systems to countries such as Iran as well as conventional armaments to countries like Sudan.
- China continues to be governed by a Communist party hierarchy that controls major aspects of the government, society, and economy. Party cadres are selected by the leadership to serve as key executives of state-owned corporations and many smaller firms and subsidiaries, and enforce the leadership policy. Beijing is also placing more party members in the ranks of newer private companies. Through this and other methods, many proliferation actions of Chinese companies are either effectively controlled or tacitly condoned by certain levels of the central government. In a number of cases, China uses proliferation to raise revenue or gain diplomatic influence.
- Continuing proliferation undermines the public commitment Beijing has made by becoming a party to, or participating in, various multilateral nonproliferation treaties, regimes, and organizations, and by promulgating strengthened export control laws.
- As China improves its nuclear and missile capabilities, the potential damage from its proliferation action increases. Given China's poor track record on preventing proliferation, the presumption is that it will continue to allow transfers of improved WMD- and missile-related technology to countries of concern.
- Numerous U.S. sanctions have been imposed to punish Chinese companies for their proliferation activities, but they appear to be largely ineffective. A significant reason for this is that many sanctions regimes do not extend penalties to a parent company, which may have business connections in the United States, for the proliferation activities of its subsidiaries unless a parent company had demonstrable knowledge of the transaction.

### **Overview**

In a post 9/11 world, addressing terrorism is of dire importance not only to the United States, but also to all in the international community. An enormous challenge is to prevent terrorist organizations, and countries that support them, from acquiring WMD and

the ability to deliver them. This should remain a central national security objective.

Unfortunately, countries of concern, such as Iran, which has been labeled a state sponsor of terrorism by the State Department, continue to receive WMD- and missile-related technology from Chinese companies. All countries, including China, should be concerned about the grave consequences should WMD be acquired by countries of concern or terrorist groups.

### **Proliferation Problems Persist**

Since the 1980s, China has been a source of billions of dollars of WMD- and missile-related technology to countries in South Asia and the Middle East.<sup>72</sup> During the 1990s, questions arose about China's compliance with its international nuclear commitments, including numerous allegations of Chinese assistance to Pakistan's nuclear program that could have had weapons-related implications.<sup>73</sup> Chinese assistance has helped Pakistan develop nuclear weapons;<sup>74</sup> Pakistan's A.Q. Khan has engaged in widespread proliferation and, for example, provided Libya with a nuclear bomb design, reportedly of Chinese origin.<sup>75</sup>

Despite the increased threat to global security, there is evidence that Chinese companies continue to transfer WMD- and missile-related equipment and technologies, including dual-use goods and technologies, to countries of concern with several Chinese firms acting as serial proliferators. According to the Director of the Defense Intelligence Agency, Vice Admiral Lowell Jacoby, "Chinese entities continue to supply key technologies to countries with WMD and missile programs, especially Pakistan, North Korea, and Iran, although China appears to be living up to its 1997 pledge to limit nuclear cooperation with Iran."<sup>76</sup> To some extent, the continuing involvement of Chinese companies with the Iranian nuclear establishment<sup>77</sup> is unsurprising, given China's openly acknowledged intention to complete work on two contracts in effect when the 1997 pledge was made. However, this contact nonetheless is troubling, given assessments that Tehran is pursuing a nuclear weapons program.<sup>78</sup> There also are concerns about Chinese companies aiding the chemical weapons programs in Iran.<sup>79</sup>

In April, September, November, and December 2004, 14 Chinese companies and one Chinese individual were sanctioned under Executive Order 12938 or the Iran Nonproliferation Act for problematic transfers. Such activity confirms that either the Chinese government's stated willingness to police this issue is disingenuous or the government lacks the power and capability to exert effective control, calling into question the value of its signature on international nonproliferation agreements. The explanation that the government lacks enforcement capability is dubious based on the effectiveness with which the government controls other activities to which it objects. In 2002, Director of Central Intelligence George Tenet testified to the Senate Armed Services Committee that some proliferation activities by Chinese companies are condoned by China's government.<sup>80</sup> In fact such activities may be paying economic and political rewards. In March 2005 Admiral Jacoby indicated that in return for sales of WMD- and missile-related technologies, China receives revenue and diplomatic influence.<sup>81</sup>

***Chinese Firms Involved in Proliferation***

As noted above, Chinese companies and individuals that transfer WMD- and missile-related equipment and technologies pose a tremendous threat to regional and global security. In some instances, as indicated in the chart below, certain large Chinese companies, or their subsidiaries, have been identified by the U.S. government as having transferred such equipment and technologies to countries of concern.

Since the Commission's 2004 Annual Report, The United States Has Placed Sanctions On The Following Companies Or Individuals. Parent Companies Are Listed In Parenthesis, <sup>82</sup> But Are Not Penalized Under These Specific Sanctions.	
<b>—CHINESE COMPANY—</b>	<b>—RECIPIENT COUNTRY—</b>
XINSHIDAI	Unnamed Country
BELJING INSTITUTE OF AERODYNAMICS (CHINA AEROSPACE SCIENCE AND TECHNOLOGY CORPORATION)	Iran
BELJING INSTITUTE OF OPTO-ELECTRONIC TECHNOLOGY	Iran
CHINA GREAT WALL INDUSTRY CORPORATION (CHINA AEROSPACE SCIENCE AND TECHNOLOGY CORPORATION)	Iran
NORTH CHINA INDUSTRIES CORPORATION (NORTH CHINA INDUSTRIES CORPORATION GROUP)	Iran
LIMMT ECONOMIC AND TRADE COMPANY, LTD	Iran
ORIENTAL SCIENTIFIC INSTRUMENTS CORPORATION (CHINA ACADEMY OF SCIENCE)	Iran
SOUTH INDUSTRIES SCIENCE AND TECHNOLOGY TRADING COMPANY, LTD	Iran
LIAONING JIAYI METALS AND MINERALS CO.	Iran
The Chinese individual CHEN QINGCHANG (aka Q.C. CHEN)	Iran
WHA CHEONG TAI COMPANY, LTD	Iran
SHANGHAI TRIPLE INTERNATIONAL, LTD	Iran
BELJING ALITE TECHNOLOGIES COMPANY, LTD	Iran
CHINA AERO-TECHNOLOGY IMPORT EXPORT CORP. (JOINTLY OWNED BY CHINA AVIATION INDUSTRIES CORPORATION I AND CHINA AVIATION INDUSTRIES CORPORATION II)	Iran
ZIBO CHEMET EQUIPMENT COMPANY, LTD	Iran

In the past five years a number of the Chinese companies that have been sanctioned by the U.S. government because of their proliferation activities have been quasi-governmental organizations, including some that have been labeled “serial proliferators.” For a full list of sanctioned companies since 1991, see Appendix A of this chapter.

The Chinese government monitors and controls functions within the state-owned industry sector and is also increasing the number of party officials assigned to private companies.<sup>83</sup> Given such connections, it is troubling that Beijing is unable or unwilling to control the proliferation activities of companies with which it has close ties. Organizations with close ties to the government that have been sanctioned for proliferation include North China Industries Corp. (NORINCO) and the China Precision Machinery Import/Export Corp. (CPMIEC).<sup>84</sup>

In some instances, sanctioned companies are subsidiaries of prominent corporate parents that do business in the United States, or with U.S. companies, or have other subsidiaries that do.<sup>85</sup> Examples include Nanjing Chemical Industries Group and Jiangsu Yongli Chemical Engineering and Technology Import/Export Corp. Both these companies have been cited by the U.S. government for exporting dual-use chemical precursors, equipment, and/or technology to Iran and have been under U.S. sanctions since 1997. Both are also subsidiaries of the Chinese oil and chemical giant Sinopec, which has conducted joint ventures with U.S. companies and raised billions of dollars in American capital markets by listing on the New York Stock Exchange, even while these two subsidiaries were under U.S. sanctions.<sup>86</sup>

Washington has often called on Beijing to scrutinize the activities of these and other companies for forbidden proliferation actions, but with limited success. According to Assistant Secretary of State Stephen Rademaker who testified before the Commission, “[Beijing’s] inability to take action against serial proliferators calls into question China’s commitment to truly curb proliferation to certain states.”<sup>87</sup>

### **Effectiveness of Chinese Export Controls**

Beginning in the early 1990s, China has taken some modest steps to address the proliferation concerns of the United States. It promised, in 1991, to abide by the Missile Technology Control Regime (MTCR) though it was passed over for MTCR membership in October 2004 presumably because of continuing exports of missile-related equipment and technology.<sup>88</sup> China also acceded to the Nuclear Nonproliferation Treaty in 1992. In December 2003, China issued its first nonproliferation white paper, calling on those involved with export license approvals to consider whether the countries receiving the controlled exports have WMD or missile programs or any links to terrorist organizations.<sup>89</sup> In keeping with this pledge, China, in recent years, has “expended considerable resources to upgrade and improve its national infrastructure for export controls.”<sup>90</sup> In September 2005, Beijing released another white paper stressing its commitments to nonproliferation.

These policies have achieved certain limited successes. In the fall of 2003, Chinese authorities intercepted a shipment of chemicals

transiting China and bound for Pyongyang's nuclear program.<sup>91</sup> In the spring of 2004, Beijing announced that it was penalizing two Chinese companies for missile-related export violations. While this was the first time China announced such sanctions, it failed to publish the identity of the guilty parties.<sup>92</sup>

One recent report by the University of Georgia's Center for International Trade and Security noted that enforcement is one of the weakest links in China's export control system and, "[h]istorically, export control enforcement in China has been opaque and half-hearted . . . its enforcement efforts still remain largely obscured."<sup>93</sup> Undoubtedly, as an expert testified to the Commission, political and economic factors "slow progress in establishing a strong, viable [export control] system."<sup>94</sup> According to an August 30, 2005 State Department report, "China's [nuclear] export control system appears designed to ensure adequate review for those exports that come to the attention of Chinese export control authorities if these authorities choose to exercise this authority."<sup>95</sup> This same report complained that "Beijing has also not taken adequate steps under these new [missile-related export control] regulations to prevent sensitive transfers or prosecute violations, and China needs to publicize its efforts to enforce its export control regulations."<sup>96</sup> According to a September 2005 report by the RAND Corporation, Beijing needs to devote more resources and political capital to improving export control practices noting that such effort "serves as a key indicator of the government's ability to fulfill its stated goal of acting like a 'responsible major power' in global affairs, especially as related to WMD nonproliferation."<sup>97</sup>

China joined the Nuclear Suppliers Group (NSG) in May 2004. Less than a month prior to joining the NSG on May 27, 2004, the Chinese government permitted the China National Nuclear Corporation to contract with Pakistan's Atomic Energy Commission to construct a second nuclear reactor at its Chasma nuclear site. China's stated policy, required under NSG guidelines, is not to export nuclear technology to a country that does not have full-scope International Atomic Energy Agency (IAEA) safeguards on all its nuclear material and facilities.<sup>98</sup> Pakistan still has not signed the IAEA's full-scope protocol on all its nuclear-related facilities. It should be noted that the new Chasma contract, signed before China's acceptance into the NSG, will be subject to a limited IAEA safeguards protocol. China's action in this case may show Beijing's proclivity to abide by the letter rather than the spirit of the law, and calls into question its commitment to nonproliferation.

Despite Beijing's rhetorical commitment to stopping impermissible transfers, Assistant Secretary of Defense for International Security Affairs Peter W. Rodman noted—

*The fact remains, however, that Chinese entities today remain key sources of transfers of arms, WMD- and missile-related equipment and technologies, including dual-use technology and related military capabilities, to countries of concern. Despite Beijing's pledges, for example, Chinese entities remain involved with the nuclear and missile efforts of Iran and Pakistan, and remain involved with chemical efforts in Iran.*<sup>99</sup>

### The U.S. Approach

Current U.S. policy toward Chinese proliferation is based on simultaneous dialogue with the Chinese government and aggressive imposition of sanctions on its companies found to be proliferating.<sup>100</sup> In January 2005, President Bush said that China has “heard us loud and clear. We will make sure to the best extent possible they do cooperate . . . We’ll make it clear not only to China, but elsewhere that we’ll hold you to account—we want to have friendly relations[,] but do not proliferate.”<sup>101</sup>

According to the former Under Secretary of State for Arms Control and International Security, John Bolton, the Bush Administration during its first term (2001–2004) sanctioned proliferating Chinese companies a total of 62 times,<sup>102</sup> although in one case those sanctions were waived on national security grounds.<sup>103</sup>

Selected U.S. Sanctions Available for Punishing Proliferating Companies:

Arms Export Control Act  
Executive Order 12938 (as amended by Executive Orders 13094  
and 13382)  
Export-Import Bank Act  
Nuclear Proliferation Prevention Act  
Export Administration Act  
Iran-Iraq Arms Nonproliferation Act  
Iran Nonproliferation Act  
Chemical and Biological Weapons Control and Warfare  
Elimination Act

One proliferation expert complained to the Commission that, “[current sanctions] are not strong enough to affect the profitability of the offending companies. Put simply, our sanctions do not have any real teeth.”<sup>104</sup> Under the provisions of most U.S. laws permitting imposition of sanctions on proliferating companies, sanctions cannot be imposed on parent companies for the proliferation activities of their subsidiaries unless the parent companies “knowingly assisted” in the prohibited transactions, a burden of proof that is very difficult to meet.<sup>105</sup>

Moreover, when a company can be sanctioned for its proliferation activities, the principal penalty is to prohibit it from conducting business with the U.S. government, and in some cases it also can be restricted from exporting its products to U.S. markets.<sup>106</sup> But the impact of such sanctions is minor because few of the proliferating companies have direct business connections with the U.S. government or substantial exports to the United States, although the parent firms may have substantial economic ties to and interests in the United States.<sup>107</sup>

The Bush Administration has aggressively used the Iran Nonproliferation Act to sanction Chinese companies for transfers of

WMD- and/or missile-related materials and technology to Iran. However, this legislation is narrowly focused and while it does provide for sanctioning successors, subunits, or subsidiaries, it does not provide for sanctioning a parent company.<sup>108</sup> In June 2001, Jiangsu Yongli Chemicals and Technology Import/Export Corp. was punished under that Act. During the period for which Jiangsu was under sanctions, its parent, the Chinese oil giant Sinopec, and some of Sinopec's other subsidiaries, benefited from joint ventures with American companies and Sinopec stock traded on the New York Stock Exchange.

On June 28, 2005, the White House issued Executive Order 13382, known as the WMD Proliferation Financing Executive Order. This order authorizes freezing U.S. assets of WMD proliferators designated under the order, thus prohibiting U.S. persons or companies from transacting business with them. According to U.S. Treasury Secretary John Snow, "[with Executive Order 13382] we deny proliferators and their supporters access to the U.S. financial system and starve them of funds needed to build deadly weapons and threaten innocents around the globe."<sup>109</sup> Denying problematic companies access to U.S. capital markets is a positive step. But under this order, parent companies can be sanctioned only on a case-by-case basis depending on the amount of their support for the actual proliferation transfers. Since it is likely to be difficult to demonstrate such support, the efficacy of applying this provision to parent companies is questionable.

Chinese companies continue to be involved in proliferation activities despite extensive bilateral dialogue in which the United States has urged China to reduce such activities, and the repeated application of sanctions to the companies found to have been involved with proliferation. The fact that many of the proliferating companies have close relationships to the Chinese government coupled with the often-observed effectiveness of the government in preventing activities it opposes, such as political dissent, confirms that the Chinese leadership's commitment to nonproliferation is insufficient. In fact, Beijing may be benefiting diplomatically from such transfers to Iran, North Korea and Pakistan.<sup>110</sup> If these activities are to be curtailed, the United States must more effectively harness multilateral diplomacy to obtain Chinese cooperation and must increase the effectiveness of its sanctions.

### **The Proliferation Security Initiative and Port Security**

In May 2003, President George W. Bush launched the Proliferation Security Initiative (PSI) aimed at halting the trafficking of WMD, delivery systems, and related materials between states or non-state actors.<sup>111</sup> France, Germany, Japan, Spain, Singapore, and the United Kingdom, among others, support the PSI which seeks to use intelligence sharing, diplomacy, joint law enforcement, and military interdictions to defeat WMD-related trafficking. Participation is voluntary and, while it has been invited to participate, China has decided not to do so, citing international law concerns in connection with interdictions. In fact, China has reportedly threatened to veto any United Nations Security Council resolution that specifically endorses the PSI.<sup>112</sup>

In addition to pursuing PSI efforts, the U.S. government also must focus more attention on U.S. port security. The dramatic increase of Chinese imports traveling through U.S. ports raises concerns about whether U.S. port security efforts are sufficient, particularly with respect to inbound container trade from China. WMD easily could enter the United States through these containers.

At the Commission's hearing in Seattle, Washington, directors of the ports of Seattle and Portland both acknowledged the scope of the problem as they discussed port security efforts underway. The Port of Portland's Nathaniel Ruda testified that U.S. ports are "at least five years from a technology solution to container seal integrity. It is a big issue."<sup>113</sup> The Port of Seattle's M.R. Dinsmore noted that only 4 to 5 percent of inbound containers are inspected and told the Commission that while the United States has "over-reacted with [regard to the security of] our nation's airports ... on the maritime side of our portfolio we've under-reacted."<sup>114</sup>

During the hearing, the Commission learned that there is limited inspection of so-called "empty" containers—those that have less than 2,000 pounds of materials in them. Also, Nathaniel Ruda conceded that fewer inspections of these empty containers are occurring now than occurred prior to 9/11, a very troubling revelation in light of the severe threat they could pose.<sup>115</sup>

Port security concerns also extend to the adequacy of screening at key foreign ports that handle outbound shipping to the United States. The Government Accountability Office (GAO) released a report on U.S. efforts to prevent nuclear smuggling via overseas seaports.<sup>116</sup> According to the report, the Department of Energy (DOE) started its Megaports Initiative in 2003 with the goal of enabling foreign personnel at key overseas ports to use U.S.-installed equipment to screen shipping containers entering and leaving these ports for nuclear and other radioactive material.<sup>117</sup> This program also coordinates with and complements the Department of Homeland Security's (DHS) Container Security Initiative (CSI), discussed below.<sup>118</sup> To assist the Megaports Initiative, Sandia National Laboratories maintains a database of foreign seaports that it considers susceptible to potential nuclear-related smuggling and which includes several Chinese ports.<sup>119</sup> The GAO found that the DOE has had limited success in initiating work in high priority foreign seaports due to difficulties in negotiating agreements with some countries including China.<sup>120</sup> The two principal reasons for these negotiating difficulties have been concerns about anticipated interruptions in the flow of commerce and reluctance to hire the additional personnel for the operation and maintenance of the U.S.-provided radiation detection equipment.<sup>121</sup> Addressing this issue should be a high priority for the DOE as well as the DHS.

While China has not agreed to the Megaports Initiative, the ports of Shenzhen and Shanghai are participating in the CSI. Under the CSI, U.S. Customs officials are stationed at the participating ports, and along with domestic agents, attempt to identify potentially dangerous cargo bound for the United States.